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MONEY

FEDERAL RESERVE BANK OF PHILADELPHIA

BUSINESS REVIEW

JUNE 1959

The Quest for Security

**The Economy at Mid-Year: More Pressure
on the Consumer**

Spotlight on Treasury Financing

Consumer Prospects in Perspective



In this space from time to time we intend to do something a little different from the articles that ordinarily take most of the lineage in the Review. These occasional pieces will not be exhaustive analyses. In fact, they may sometimes be merely intriguing ideas that need further investigation. Or they may express a point of view. Or they may explain the Federal Reserve's position on some matters under current discussion. In short, we intend to be flexible. Any comments will be welcomed.

THE QUEST FOR SECURITY



An old saw has it that in our kind of economy "the consumer is king." Like most such sayings, it is a cliché because it is true. This issue of the Review recognizes the importance of the consumer by discussing two aspects of his behavior: his short-run actions since the recession, and his longer-run decisions as to whether to spend or save. As both articles indicate, the consumer will have a lot to say about our economic well-being in both the short and longer run.

But in the end the consumer may have a bigger impact on our destinies, not as he decides what he wants, but as he decides how he intends to get it. When we say that the consumer is king, we usually think of the textbook explanation: assume free competitive markets; the consumer makes known his desires for various goods by bidding certain prices; these prices attract or repel the use of economic resources to or away from production of various goods; hence, the consumer directs resources.

Yet there is another way that we as consumers can express our desires and direct resources—and we are all consumers in the sense that we all consume, in one way or another, the total goods and services produced. This is by

(Continued on Page 13)

THE ECONOMY AT MIDYEAR:



MORE PRESSURE ON THE CONSUMER

By now it is clear that business conditions in the first half of 1959 exceeded expectations of the majority and matched the most optimistic projections made at the turn of the year. Overall measures of activity all show substantial advances. What is more, sharp recovery in the over-all totals is not the result of just a few areas of activity booming. Rather it reflects a surge in numerous and diversified segments of the economy. Practically everyone who sells anything from cars to carpet tacks is doing better this year.

Because the totals are higher, and because the recovery seems broad-based, it is tempting to be swept along in a wave of optimism. Some current writing assures us that the recovery has been well balanced and the prosperity period ahead will be stronger and longer as a result. Maybe this is true. But at the risk of sounding pessimistic, it might be well to point out some things that aren't currently being emphasized elsewhere.

A well balanced recovery?

"Well balanced" is considered a favorable label when applied to almost anything. Sports writers call a pennant favorite well balanced. Our diets should be well balanced. Corporations strive for a well balanced management team. Even motor oils advertise that they are well balanced.

So it is in economics. We are told this recovery has been well balanced; so it should be followed by a long, strong period of prosperity. How long is long and how strong is strong? Well, probably longer and stronger than that which followed the 1954 recession.

It is difficult, if not impossible, to be precise about balance in an economy. In broadest terms, perhaps, balance in a free economy is conveniently measured by price indices. And indeed the recent stability in prices is considered by some to be important evidence of the smooth working of our economy in recovery.

But there are at least two things to keep in mind about prices as a signal of a balanced

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economy: (1) Price movements may no longer accurately reflect what is happening in the economy; (2) price behavior is little different from that which followed the 1954 recession.

The consumer and wholesale price indices are assumed to act as thermometers for the economy. When they register higher, demand is becoming excessive; when they decline, supply is redundant; and when they are stable, supply and demand are pretty much in balance.

But in late 1957 and early 1958, when demand was falling and the economy was obviously in a recession, prices were rising. From this experience it is possible to theorize that price indices are not the reliable indicators they once were. Changes in our economy probably have rendered them less sensitive. They give sluggish and sometimes inaccurate indications.

Sometimes memories play tricks on us. At present there seems to be a common notion that price indices show more stability now than at a comparable point following the 1954 recession. Actually, this isn't the case. In April 1958, at the bottom of the recession the consumer price index stood at 123.5. A year later the index registered 123.9. The 1954 recession bottom was touched in August. At that time the consumer

price index was 115.0. One year later the index was 114.5.

As can be seen from the chart, the wholesale price index has followed a similar course in the aftermath of each recession. No support is given to those who purport to see "better balance" from the movements in the price indices. In both periods both indices moved within a narrow range.

The feeling that this has been a well balanced recovery rests on factors in addition to stability in the price indices. The aforementioned fact that there has been a surge in numerous and diversified segments of the economy lends support to this feeling.

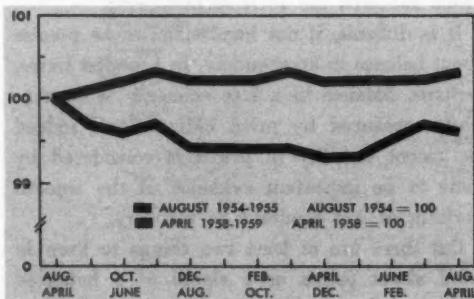
It is impossible to be anything but impressed with the depth and breadth of the recovery in nearly all lines of activity. Retail stores of all kinds are ringing up higher sales totals. Manufacturers have hiked production schedules. Construction firms are doing more building. Mine operators are busier.

These developments are less impressive, however, when matched against the pattern of comeback following the 1954 recession. The same broad, deep-seated resurgence was apparent from the figures. The same feeling of balanced, healthy recovery must have been conveyed. In fact, it has nearly always been the case that in the aftermath of recession a broad resurgence takes place.

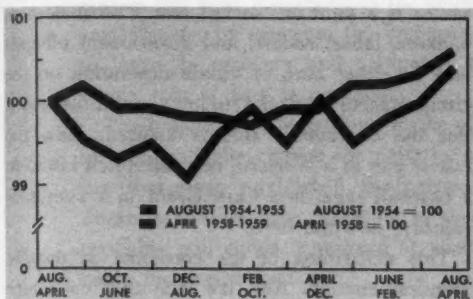
Government spending and steel negotiations

This is not to say that there are no differences between this recovery to date and what happened after the 1954 recession. There are many differences. Perhaps most important have been: (1) The larger part that government spending has played; and (2) the fillip provided demand by the impending steel negotiations.

CONSUMER PRICES



WHOLESALE PRICES



Government expenditures since the low quarter of the recession have grown by 9.4 per cent. During a comparable period in the 1954-1955 upturn, government spending rose less than 1 per cent. All other major types of spending except spending for inventory have risen less rapidly than in the comparable period in 1954-1955.

Personal consumption expenditures in the last recovery gained 7.5 per cent, as compared with just 5.0 per cent this time. In fact, spending rose more rapidly than income in 1954-1955, but has fallen short in this recovery. Each major category of consumer spending—durables, nondurables, and services—has bounced back more slowly this time. Spending on durable goods—cars, appliances, furniture, etc.—is only about one-half as sizable as the 21 per cent jump in the 1954-1955 period.

Residential housing outlays and plant and equipment spending similarly showed larger gains at this stage of the 1954-1955 recovery. When these categories of spending are combined with inventory spending to form private domestic investment, however, the present over-all gain measures 38 per cent compared with a gain of 34 per cent in the earlier upturn.

Obviously, the switch from a heavy rate of

inventory reduction to stockpiling in the present recovery is sufficiently large to offset the slower gains in housing outlays and plant and equipment spending. Of course, a part of the spurt in inventory accumulation must be ascribed to the unusually heavy demand for steel. The possibility of a strike in that industry undoubtedly induced steel users to stockpile more than they would otherwise.

From the above, it could be concluded that this recovery might have been less rapid were it not for the strong surge in government spending and "strike-induced" stockpiling. This conclusion derives significance from the observation that probably neither of these forces will be working so strongly in the near future.

The increase in total government spending began to slow in the first quarter of this year. For the foreseeable future it appears as if total government spending will recede slightly in importance. It will not form quite so large a part of gross national product as it does at present.

Similarly, inventory accumulation will probably assume a lesser role in the future. This is not to say that inventory build-up is over. All the signs indicate it is just beginning. But the artificialities injected into stockpiling by the strike threat will be soon ended. In addition, the original change from decumulation to accumulation usually provides the greatest fillip to demand.

Capital spending and housing

It is apparent that private demand—except for inventory accumulation—has so far played a smaller role and government spending for goods and services a much larger one than was the case in the 1954-1955 upsurge. It is just as apparent that private demand now is going to have to assert itself.

What are the prospects? Will private demand rise to the occasion? Will it drive us through a new period of prosperity longer and stronger than the preceding?

Even a tentative answer to this question requires that each of the major aspects of private demand be examined individually. Since inventory prospects already have been appraised it is convenient to look first at the other major components of private domestic investment.

Investment spending in new plant and equipment moved higher in the first quarter of this year. Preliminary indications are that the upward slant will continue through the second quarter. Surveys of planned capital spending indicate slight gains through the balance of the year. It is possible however, that a surge in consumer spending for durables would bring forth a significantly higher level of capital spending than now foreseen. Experience shows there has been a tendency to underestimate the strength of capital spending when the economy is rising. Certainly corporate coffers appear to be in a ready-to-spend position.

Spending for residential housing has been rising rapidly in the recent past. (Only a very little less rapidly than over a comparable period in 1954-1955.) The consensus has it that this spending will slow somewhat as money conditions tighten. Possibly spending on residential housing won't rise much from current levels. At the same time, it is a good bet that no really large decline in this spending will take place in the near future.

What this all seems to mean is that how fast over-all activity increases will depend more on what the consumer does than it has in the past.

Enter the consumer

Everyone who writes about business conditions

learns very early in the game that the consumer is a kind of "sacred cow." Businessmen, bankers, labor leaders, and government officials may be either hero or villain depending on the circumstances and the writer's point of view. But the consumer's role is assured. He's the fastest gun in a Western, he's the clutch hitter in a baseball saga, he's Cary Grant in a romantic comedy, he's the hero.

This enshrining of the consumer is usually harmless enough. And it's true that consumer spending is tremendously important. Arithmetically it is twice as important as government and business combined. Sometimes, however, by enshrining the consumer we inhibit understanding of what is going on.

For example, currently there is a tendency to overemphasize the role the consumer played in "seeing us through" the recession and bringing about recovery. It's true indeed that consumers maintained spending at a fairly high level even in the face of the recession. It's also true—and not nearly so well publicized—that unemployment benefits, high dividends despite declining profits, union welfare benefits, and easier money helped the consumer maintain spending.

Again, for the most part, there seems little harm in the de-emphasis given these "little helps" provided the consumer. And everyone could go along enjoying this little delusion except for one thing. It is giving us a false impression of what the consumer can and will do. We are beginning to ascribe powers to him that he may not possess.

With more of the burden for economic advance resting on the consumer, how likely is it that his spending will increase rapidly?

Consumer spending on food and clothing has risen in 27 of the last 30 measured quarters. Spending on services has been higher each

quarter for 62 in a row. The size of the increases has been responsive to the general business climate. In recession the increases are not so large. In recovery and prosperity a larger, steady rate of gain is resumed.

There appears to be nothing in the offing that will dramatically change the patterns of spending that have established themselves in nondurables and services. Spending in these forms probably will continue upward at what has become the accustomed rate.

Every one agrees the pick-up in speed, if it is to come, will have to occur largely in spending for durable goods. This kind of spending traditionally pursues a much more erratic course than other forms of consumer spending. It is capable of dramatic short-run changes in volume and direction.

Consumer spending on durables already has picked up considerably from recession lows. That it hasn't gained so much as in 1954-1955 almost seems to be the principal reason why a further surge is anticipated. Of course, a new surge in spending could occur. The consumer

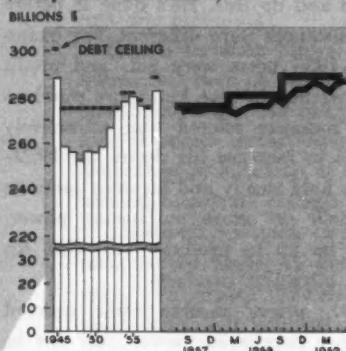
could hike his propensity to consume and carry the economy on to new high ground.

The point is, however, ordinarily he does not just go ahead and do this. He's done it before but the circumstances were different. For example, in 1954-1955 taxes were cut, and credit terms were stretched to give him more purchasing power. Producers offered him attractively restyled goods to increase his desire. In 1959-1960 if prices hold steady and incomes continue to increase he'll get more purchasing power. Then it will be up to producers to whet his appetite with attractive products.

If, however, prices resume their upward climb, consumer purchasing power may not be adequate to spark a surge in buying. It will do no good if incomes increase and prices do too. With all the recovery that has taken place the economy is only about where it was two years ago and there are six million more people to provide for. Per capita real spending power is not so high as it was. Probably it will have to rise if consumer spending is to drive the economy through a longer, stronger prosperity.

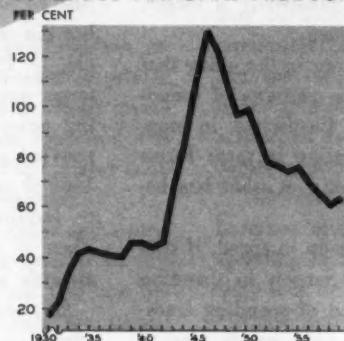
SPOTLIGHT ON TREAS

OUTSTANDING FEDERAL DEBT (Subject to Limitation)



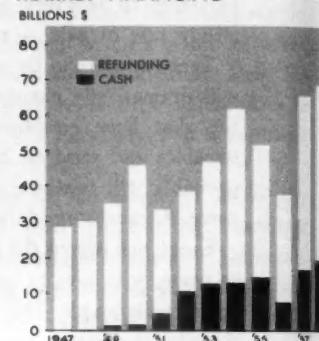
1. The volume of Federal debt has been rising.

FEDERAL DEBT AS A PERCENTAGE OF GROSS NATIONAL PRODUCT



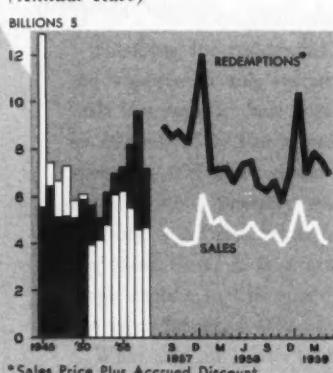
2. Compared with Gross National Product, however, the debt has declined. The ratio increased in 1958, but with the economy advancing, it should decline again.

VOLUME OF MARKET FINANCING



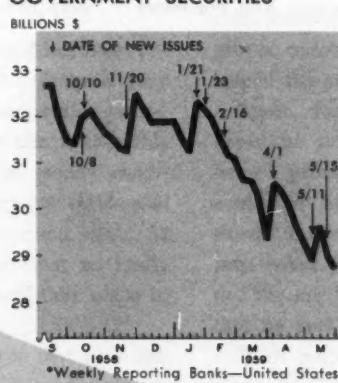
3. In some ways more important than the level of the debt is the volume of funds raised in the market. Last year, it totaled about \$70 billion (not including the weekly rollover of some \$2 billion of bills).

SAVINGS BONDS (Annual Rate)



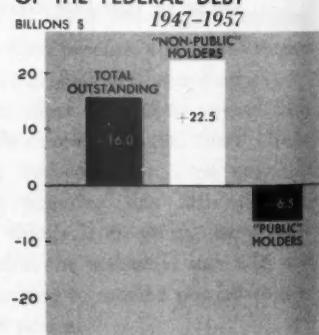
7. Individuals have been redeeming more savings bonds than they have been buying.

BANK HOLDINGS OF GOVERNMENT SECURITIES*



8. Fears that purchases by commercial banks during the recent recovery period would inflate the money supply have not been borne out. Bank purchases of new issues were subsequently sold to other investors.

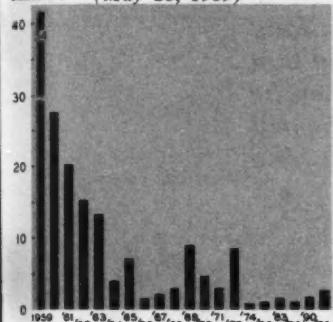
CHANGING OWNERSHIP OF THE FEDERAL DEBT 1947-1957



9. Shifting ownership of the debt can have varying impacts on the market. The increase in the Federal debt from 1947-1957 (excluding savings bonds) was absorbed by 'non-public' sources (mainly Government agencies and trust funds).

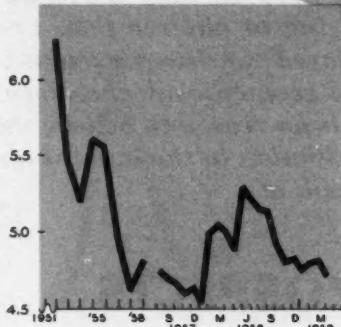
TREASURY FINANCING

MATURITY SCHEDULE OF
MARKETABLE SECURITIES
(May 26, 1959)



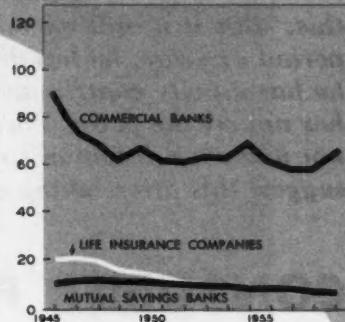
4. One reason for the high level of market activity is the large volume of issues coming due within one year.

AVERAGE MATURITY
OF MARKETABLE DEBT
YEARS



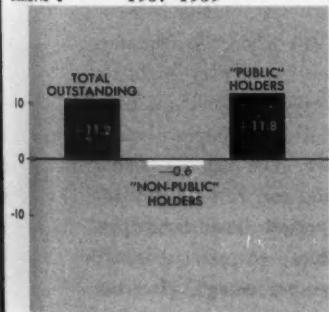
5. The average maturity of the debt has lengthened during recent recessions and shortened during the 1955-1957 boom and the current recovery.

HOLDINGS OF
GOVERNMENT SECURITIES
BILLIONS \$



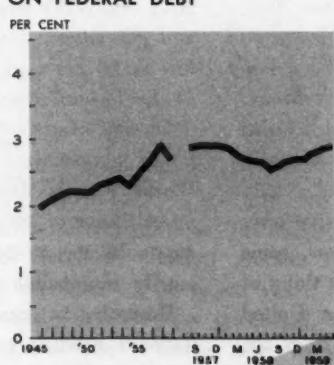
6. Since World War II major institutional investors have reduced their holdings of Government securities.

CHANGING OWNERSHIP
OF THE FEDERAL DEBT
1957-1959



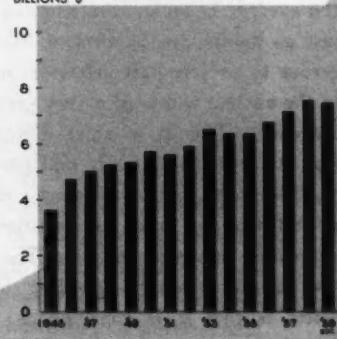
10. But the increase in Federal debt from 1957-April 1959 was absorbed by the "public" (largely corporations, commercial banks, state and local governments, etc.). Issues had to be made more attractive in order to appeal to these investors.

INTEREST RATE
ON FEDERAL DEBT



11. The average interest paid on the debt has been rising.

TOTAL INTEREST
ON FEDERAL DEBT
(Fiscal Years)



12. The amount of interest paid on the debt has about doubled since World War II.



In the previous article we have emphasized the strategic importance of the consumer in the coming months. It would be no mean accomplishment for the consumer to propel the economy today as he did in 1955. He may not be up to doing this. But it is still encouraging to observe that, over a long period of years, he has displayed consistent strength; and that he has usually contributed to economic advance even when he has not set the pace. There is no reason to believe that he will not make a substantial contribution in the months ahead. We suggest this after taking a look at . . .

CONSUMER PROSPECTS IN PERSPECTIVE



Can we judge the future by the past? Sometimes. Can we tell what role the consumer will play in the current economic expansion by looking at his past performance? Perhaps. Of course, temporary influences often distort long-run average behavior. Patterns can be destroyed just as habits can be broken. It's always dangerous to project past behavior into the future. In the ancient words of a very practical Scottish preacher, "This is a great difficulty. We will look it in the face boldly and pass on."

At least the consumer has an extensive past, as statistics go; and, as statistics show, some interesting habits of behavior. The first thing of note about consumer spending in the United States is that it is conspicuous. In 1958 the American consumer purchased over \$290 billion worth of clothing, food, automobiles, haircuts, and the like. This represents more hardware and more software than any group of people have ever bought at any time, anywhere.

The proportion of gross national product consumers have purchased has fluctuated rather widely over the last 50 years. It has been as high as 80 per cent in the depression years of 1932 and 1933 when the demands of business and government were very low. It has been as low as 48 per cent in 1944 when the demands of the Federal Government were very high.

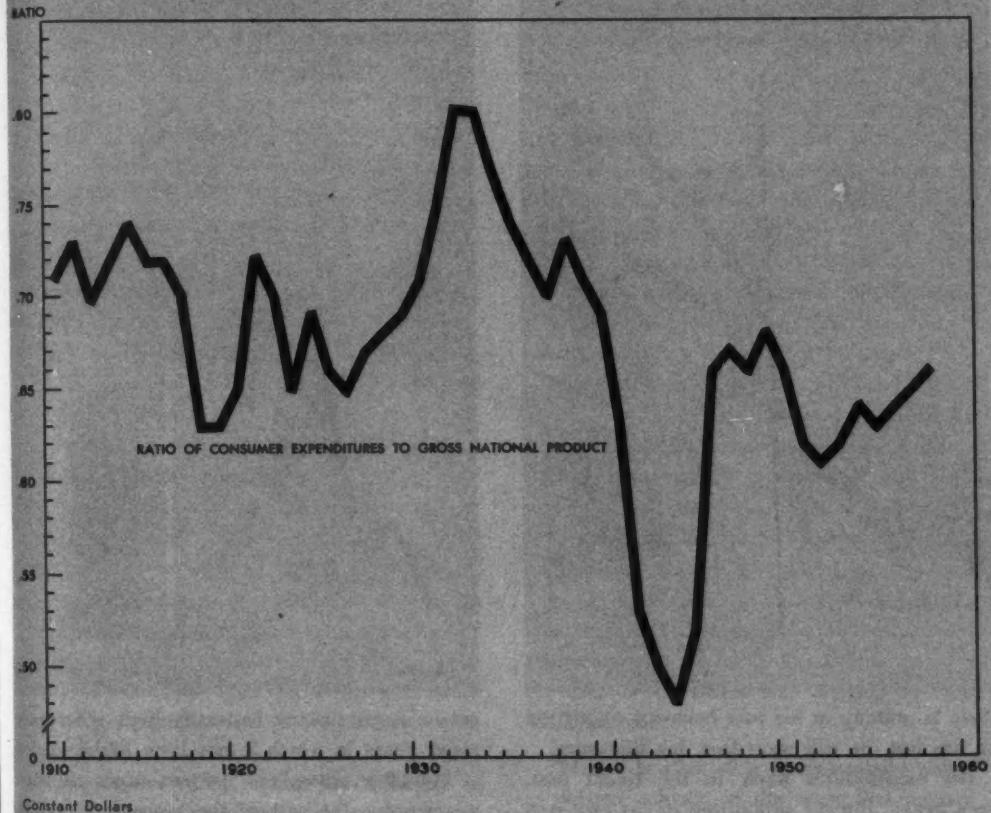
On the average, the consumer took an even larger proportion of national output before World War II than after. The rapidly rising expenditures of local, state, and Federal governments in the postwar period have been primarily responsible for this.

Recently, however, the percentage of gross national product taken by the consumer has been steadily increasing. Between 1952 and 1958, it increased by over 8 per cent.

This reflects the fact that consumer expenditures over the past six years have been rising faster than gross national product. The con-

THE CONSUMERS' SHARE OF G.N.P.

The share of gross national product purchased by consumers has fluctuated widely over the years. However, it has been rising since 1952.



Constant Dollars

sumer has been able to push up his share of gross national product by expanding his expenditures very rapidly—even more rapidly than his own personal income has increased. If you aren't saving any more today than six years ago, even though your income is larger, you have lots of company.

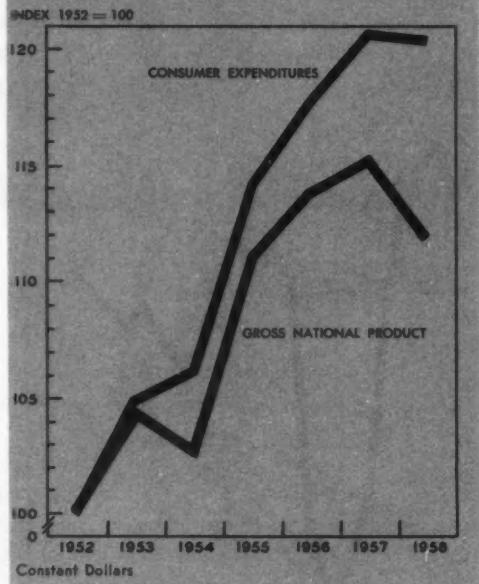
The consumer, then, has been a "most important fellow." The proportion of gross na-

tional product that he has been purchasing in recent years, though not the highest he has ever purchased, is greater than the combined shares taken by both business and government; and his large share has been increasing over the past six years.

It is difficult to say exactly what the consumer will do in the next week, the next month, or the next year. But perhaps it is helpful to know that

RECENT CONSUMER BEHAVIOR: SPENDING PATTERNS

The increasing portion of production taken by consumers over the past six years reflects the fact that consumer expenditures have been rising faster than gross national product.

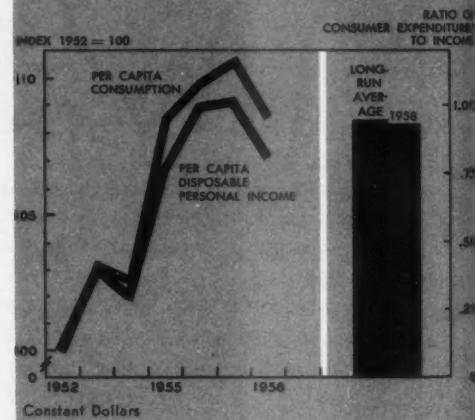


there is nothing in his past behavior to suggest he has lost, or will soon lose, his buoyancy.

His expenditures have, in the recent past, been heavy. But the proportion of his own personal income that he is now spending is not unusually high when compared to previous years—in fact it is not quite up to the long-run average of about 94 per cent. Nor, for that matter, is the proportion of gross national prod-

The consumer has been able to increase his share of the total national output of goods and services by increasing his expenditures very rapidly—even more rapidly than his own income has increased.

Despite this hard spending, consumer expenditures as a proportion of consumer income in 1958 were still somewhat below the long-run average.



uct he is purchasing unusually high—there are many years in which it has been higher.

Moreover, if any "one" pattern stands out when we examine the past of the average American consumer, it is his consistently high level of spending. It appears that while he may become indifferent to one or several kinds of products, he does not get tired of all products. His wants seem to expand with his ability to satisfy them.

The Quest for Security

(Continued from Page 2)

the political, rather than economic, process. We have been getting what we want increasingly through Government, both by having Government buy a larger share of our total output and by having Government give us various kinds of aid and support.

Now, this path of events has many implications, and there is space to go into only one of them here. This is the question of how we as individuals have been trying to make ourselves economically secure.

Since these efforts naturally have a strong influence on the environment in which monetary authorities formulate and execute policy, the President of this Bank recently has addressed himself to the subject of "The Quest for Security."* Here are some excerpts from his speech:

"The search for security is as old as mankind. Like happiness, security probably is never achieved by the individual who pursues it directly. In all probability it is a by-product of seeking something more significant. Surely the citizens of the United States are economically more secure today than their forebears were a couple of centuries ago; yet I am not aware that they actually feel more secure, even economically. . . .

"Individual security cannot be achieved in isolation. It must be related to the total environment. Individual security will become meaningless if we stop growing and if prices keep rising. Unfortunately, we have not always recognized this. Too frequently we have sought personal security on an exclusive, personal basis. We have sought security in our particular job and our particular activity. When the market for our particular product or service has weakened,

we have asked the Government to support it. . . .

"How can . . . [monetary policy] contribute to security—to growth without inflation? In this area, as in the others I have described, we must see the individual, not in isolation but as part of the total picture. Ask an individual what he would need to solve his material problems. His simple answer might well be: 'More money.' And, of course he would be right—so long, that is, as he alone had additional money.

"Unfortunately, however, this effective answer for any single individual is no answer for all individuals collectively. The individual could solve his material problem with more money because it would enable him to take more resources out of the common pool, thereby leaving less for others. All individuals collectively, however, cannot take more out of the pool of resources than is in that pool—no matter how much money they may have. Society must produce more, not merely have more money, before it can consume and invest more.

"I should like to introduce a discussion of the positive role of monetary policy with a quotation from that venerable Cambridge economist, Sir Dennis H. Robertson. Writing in March 1921, he said:

"Money is after all a fundamentally unimportant subject, in the sense that neither the most revolutionary nor the 'soundest' monetary policy can be expected to provide a remedy for those strains and disharmonies whose roots lie deep in the present structure of industry, and perhaps in the very nature of man himself."

"What monetary policy can do is to influence the environment in which economic decisions are made rather than determine the particular

*Address before the 56th Annual Convention of the New Jersey Bankers Association, Atlantic City, N. J., May 21, 1959.

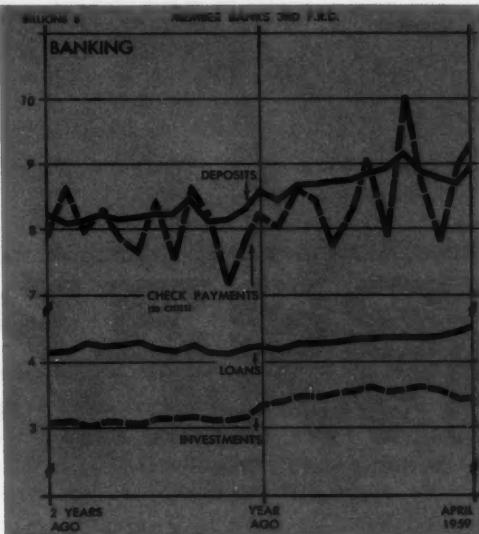
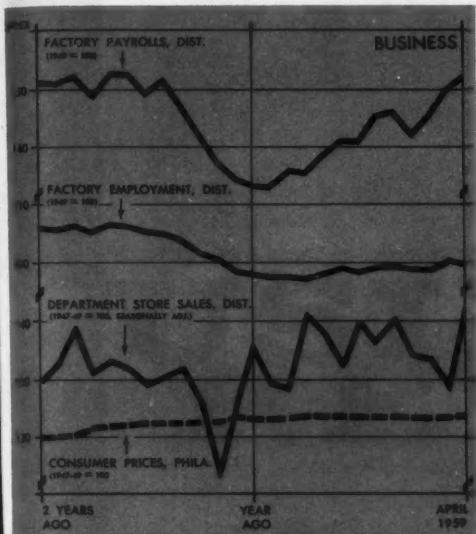
decisions themselves. It can provide incentives to spend on consumption and investment when the economy has unused resources that are not idle for structural reasons; and it can provide incentives to save when the economy wishes to consume and invest more than it can produce.

"The Federal Reserve System provides these incentives by making money and credit relatively cheap and plentiful to encourage spending and by making it relatively dear and scarce to encourage saving. . . .

"You may recall that in the Employment Act

of 1946, Congress declared that the goals of maximum employment, production, and purchasing power should be achieved 'in a manner calculated to foster and promote free competitive enterprise.' Those words are significant. There are individual satisfactions and social rewards deriving from an economic system that permits individuals to succeed and advance in society on their foresight and efficiency. This is the framework in which we search for security. We strive not for the security of slaves but for the security of free men."

FOR THE RECORD...



SUMMARY	Third Federal Reserve District		United States				LOCAL CHANGES	Factory*		Department Store†		Check Payments	
	Per cent change		Per cent change					Employment	Payrolls	Sales	Stocks		
	Apr. 1959 from mo. ago		4 mos. 1959 from year ago		Apr. 1959 from mo. ago			Per cent change Apr. 1959 from mo. ago	Per cent change Apr. 1959 from year ago	Per cent change Apr. 1959 from mo. ago	Per cent change Apr. 1959 from year ago		
	year ago		year ago		year ago			mo. ago	year ago	mo. ago	year ago		
OUTPUT													
Manufacturing production	+ 1	+ 7	+ 3	+ 1	+ 19	+ 14							
Construction contracts	-22	0	+23	+13	+31	+22							
Coal mining	+ 6	+11	+11	0	+13	+ 5							
EMPLOYMENT AND INCOME													
Factory employment (Total)	0	+ 2	0	0	+ 6	+ 2							
Factory wage income	+ 1	+14	+ 8	0	0	0							
TRADE*													
Department store sales	+10	+ 5	+ 7	+ 1	+ 8	+ 8							
Department store stocks	+ 1	+ 4	0	+ 2	+ 6	0							
BANKING (All member banks)													
Deposits	+ 2	+ 4	+ 6	+ 2	+ 3	+ 6							
Loans	+ 1	+ 6	+ 6	+ 2	+ 8	+ 6							
Investments	0	+ 3	+10	+ 1	+ 2	+ 9							
U.S. Govt. securities	0	+ 3	+11	+ 1	0	+ 9							
Other	0	+ 4	+ 8	+ 2	+ 8	+11							
CHECK PAYMENTS													
Wholesale	0	+ 1	+ 1	0	+ 1	0							
Consumer	0	+ 1	+ 1	0	0	+ 1							

*Adjusted for seasonal variation. †20 Cities ‡Philadelphia

*Not restricted to corporate limits of cities but covers areas of one or more counties.

†Adjusted for seasonal variation.

